

AMENDED IN SENATE APRIL 7, 2005

SENATE BILL

No. 790

Introduced by Senator Speier

February 22, 2005

~~An act to relating to lending.~~ *An act to amend Sections 4970 and 4973 of the Financial Code, relating to lending.*

LEGISLATIVE COUNSEL'S DIGEST

SB 790, as amended, Speier. ~~Uniformity in lending practices~~
Covered loans.

Existing law imposes various prohibitions and limitations on certain loans, defined as covered loans, including prohibiting a prepayment penalty after the first 36 months after the date of the consummation of the loan.

This bill would revise the definition of a covered loan. The bill would instead prohibit a prepayment penalty after the first 12 months after the date of the consummation of the loan. The bill would require a borrower to be offered loan counseling and sign a certification that he or she has received or waived the counseling before a covered loan may be made.

~~Existing law provides for the regulation of finance lenders and residential mortgage lenders by the Department of Corporations.~~

~~This bill would state that it is the intent of the Legislature that equitable terms of lending be available to residents of each city and county in California.~~

Vote: majority. Appropriation: no. Fiscal committee: ~~no~~ yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

~~SECTION 1. It is the intent of the Legislature that equitable terms of lending be available to residents of each city and county in California.~~

SECTION 1. Section 4970 of the Financial Code is amended to read:

4970. For purposes of this division:

(a) “Annual percentage rate” means the annual percentage rate for the loan calculated according to the provisions of the federal Truth in Lending Act and the regulations adopted thereunder by the Federal Reserve Board.

(b) ~~(+)~~ “Covered loan” means a consumer loan in which the original principal balance of the loan does not exceed ~~two hundred fifty thousand dollars (\$250,000)~~ *the current conforming first mortgage loan size limit for a single-family dwelling as established by the Federal National Mortgage Association* in the case of a mortgage or deed of trust, and where one of the following conditions are met:

~~(A)~~

(1) For a mortgage or deed of trust, the annual percentage rate at consummation of the transaction will exceed by more than eight percentage points the yield on Treasury securities having comparable periods of maturity on the 15th day of the month immediately preceding the month in which the application for the extension of credit is received by the creditor.

~~(B)~~

(2) The total points and fees payable by the consumer at or before closing for a mortgage or deed of trust will exceed 6 percent of the total loan amount.

~~(2) The dollar amount specified in paragraph (1) shall be adjusted every five years in accordance with the California Consumer Price Index.~~

(c) “Points and fees” shall include the following:

(1) All items required to be disclosed as finance charges under Sections 226.4(a) and 226.4(b) of Title 12 of the Code of Federal Regulations, including the Official Staff Commentary, as amended from time to time, except interest.

1 (2) All compensation and fees paid to mortgage brokers in
2 connection with the loan transaction, *including, but not limited*
3 *to, the payment of yield spread premiums.*

4 (3) All items listed in Section 226.4(c)(7) of Title 12 of the
5 Code of Federal Regulations, only if the person originating the
6 covered loan receives direct compensation in connection with the
7 charge.

8 (4) *Any prepayment fees required to be paid by the borrower.*

9 (d) “Consumer loan” means a consumer credit transaction that
10 is secured by real property located in this state used, or intended
11 to be used or occupied, as the principal dwelling of the consumer
12 that is improved by a one-to-four residential unit. “Consumer
13 loan” does not include a reverse mortgage, ~~an open line of credit~~
14 ~~as defined in Part 226 of Title 12 of the Code of Federal~~
15 ~~Regulations (Regulation Z),~~ or a consumer credit transaction that
16 is secured by rental property or second homes. “Consumer loan”
17 does not include a bridge loan. For purposes of this division, a
18 bridge loan is any temporary loan, having a maturity of one year
19 or less, for the purpose of acquisition or construction of a
20 dwelling intended to become the consumer’s principal dwelling.

21 (e) “Original principal balance” means the total initial amount
22 the consumer is obligated to repay on the loan.

23 (f) “Licensing agency” shall mean the Department of Real
24 Estate for licensed real estate brokers, the Department of
25 Corporations for licensed residential mortgage lenders and
26 licensed finance lenders and brokers, and the Department of
27 Financial Institutions for commercial and industrial banks and
28 savings associations and credit unions organized in this state.

29 (g) “Licensed person” means a real estate broker licensed
30 under the Real Estate Law (Part 1 (commencing with Section
31 10000) of Division 4 of the Business and Professions Code), a
32 finance lender or broker licensed under the California Finance
33 Lenders Law (Division 9 (commencing with Section 22000)), a
34 residential mortgage lender licensed under the California
35 Residential Mortgage Lending Act (Division 20 (commencing
36 with Section 50000)), a commercial or industrial bank organized
37 under the Banking Law (Division 1 (commencing with Section
38 99)), a savings association organized under the Savings
39 Association Law (Division 2 (commencing with Section 5000)),
40 and a credit union organized under the California Credit Union

1 Law (Division 5 (commencing with Section 14000)). Nothing in
2 this division shall be construed to prevent any enforcement by a
3 governmental entity against any person who originates a loan and
4 who is exempt or excluded from licensure by all of the licensing
5 agencies, based on a violation of any provision of this division.
6 Nothing in this division shall be construed to prevent the
7 Department of Real Estate from enforcing this division against a
8 licensed salesperson employed by a licensed real estate broker as
9 if that salesperson were a licensed person under this division. A
10 licensed person includes any person engaged in the practice of
11 consumer lending, as defined in this division, for which a license
12 is required under any other provision of law, but whose license is
13 invalid, suspended or revoked, or where no license has been
14 obtained.

15 (h) “Originate” means to arrange, negotiate, or make a
16 consumer loan.

17 (i) “Servicer” has the same meaning provided in Section 6
18 (i)(2) of the Real Estate Settlement Procedures Act of 1974.

19 *SEC. 2. Section 4973 of the Financial Code is amended to*
20 *read:*

21 4973. The following are prohibited acts and limitations for
22 covered loans:

23 (a) (1) A covered loan shall not include a prepayment fee or
24 penalty after the first—~~36~~ 12 months after the date of
25 consummation of the loan.

26 (2) A covered loan may include a prepayment fee or penalty
27 up to the first—~~36~~ 12 months after the date of consummation of the
28 loan if:

29 (A) The person who originates the covered loan has also
30 offered the consumer a choice of another product without a
31 prepayment fee or penalty.

32 (B) The person who originates the covered loan has disclosed
33 in writing to the consumer at least three business days prior to
34 loan consummation the terms of the prepayment fee or penalty to
35 the consumer for accepting a covered loan with the prepayment
36 penalty and the rates, points, and fees that would be available to
37 the consumer for accepting a covered loan without a prepayment
38 penalty.

39 (C) The person who originates the covered loan has limited the
40 amount of the prepayment fee or penalty to an amount not to

1 exceed the payment of six months' advance interest, at the
2 contract rate of interest then in effect, on the amount prepaid in
3 any 12-month period in excess of 20 percent of the original
4 principal amount.

5 (D) A covered loan will not impose the prepayment fee or
6 penalty if the covered loan is accelerated as a result of default.

7 (E) The person who originates the covered loan will not
8 finance a prepayment penalty through a new loan that is
9 originated by the same person.

10 (b) (1) A covered loan with a term of 5 years or less may not
11 provide at origination for a payment schedule with regular
12 periodic payments that when aggregated do not fully amortize the
13 principal balance as of the maturity date of the loan.

14 (2) For a payment schedule that is adjusted to account for the
15 seasonal or irregular income of the consumer, the total
16 installments in any year shall not exceed the amount of one
17 year's worth of payments on the loan. This prohibition does not
18 apply to a bridge loan. For purposes of this paragraph, "bridge
19 loan" means a loan with a maturity of less than 18 months that
20 only requires payments of interest until the time when the entire
21 unpaid balance is due and payable.

22 (c) A covered loan shall not contain a provision for negative
23 amortization such that the payment schedule for regular monthly
24 payments causes the principal balance to increase, unless the
25 covered loan is a first mortgage and the person who originates
26 the loan discloses to the consumer that the loan contains a
27 negative amortization provision that may add principal to the
28 balance of the loan.

29 (d) A covered loan shall not include terms under which
30 periodic payments required under the loan are consolidated and
31 paid in advance from the loan proceeds.

32 (e) A covered loan shall not contain a provision that increases
33 the interest rate as a result of a default. This provision does not
34 apply to interest rate changes in a variable rate loan otherwise
35 consistent with the provisions of the loan documents, provided
36 the change in the interest rate is not triggered by the event of
37 default or the acceleration for the indebtedness.

38 (f) (1) A person who originates covered loans shall not make
39 or arrange a covered loan unless at the time the loan is
40 consummated, the person reasonably believes the consumer, or

1 consumers, when considered collectively in the case of multiple
2 consumers, will be able to make the scheduled payments to repay
3 the obligation based upon a consideration of their current and
4 expected income, current obligations, employment status, and
5 other financial resources, other than the consumer's equity in the
6 dwelling that secures repayment of the loan. In the case of a
7 covered loan that is structured to increase to a specific designated
8 rate, stated as a number or formula, at a specific predetermined
9 date not exceeding 37 months from the date of application, this
10 evaluation shall be based upon the fully indexed rate of the loan
11 calculated at the time of application.

12 The consumer shall be presumed to be able to make the
13 scheduled payments to repay the obligation if, at the time the
14 loan is consummated, the consumer's total monthly debts,
15 including amounts owed under the loan, do not exceed 55 percent
16 of the consumer's monthly gross income, as verified by the credit
17 application, the consumer's financial statement, a credit report,
18 financial information provided to the person originating the loan
19 by or on behalf of the consumer, or any other reasonable means.

20 (2) No presumption of inability to make the scheduled
21 payments to repay the obligation shall arise solely from the fact
22 that at the time the loan is consummated, the consumer's total
23 monthly debts, including amounts owed under the loan, exceed
24 55 percent of the consumer's monthly gross income.

25 (3) In the case of a stated income loan, the reasonable belief
26 requirement in paragraph (1) shall apply, however, for stated
27 income loans that belief may be based on the income stated by
28 the consumer, and other information in the possession of the
29 person originating the loan after the solicitation of all information
30 that the person customarily solicits in connection with loans of
31 this type. A person shall not knowingly or willfully originate a
32 covered loan as a stated income loan with the intent, or effect, of
33 evading the provisions of this subdivision.

34 (g) A person who originates a covered loan shall not pay a
35 contractor under a home-improvement contract from the
36 proceeds of a covered loan other than by an instrument payable
37 to the consumer or jointly to the consumer and the contractor or,
38 at the election of the consumer, to a third-party escrow agent for
39 the benefit of the contractor in accordance with terms and
40 conditions established in a written escrow agreement signed by

1 the consumer, the person who originates a covered loan, and the
2 contractor prior to the disbursement of funds. No payments, other
3 than progress payments for home-improvement work that the
4 consumer certifies is completed, shall be made to an escrow
5 account or jointly to the consumer and the contractor unless the
6 person who originates the loan is presented with a signed and
7 dated completion certificate by the consumer showing that the
8 home-improvement contract was completed to the satisfaction of
9 the consumer.

10 (h) It is unlawful for a person who originates a covered loan to
11 recommend or encourage a consumer to default on an existing
12 consumer loan or other debt in connection with the solicitation or
13 making of a covered loan that refinances all or any portion of the
14 existing consumer loan or debt.

15 (i) A covered loan shall not contain a call provision that
16 permits the lender, in its sole discretion, to accelerate the
17 indebtedness. This prohibition does not apply if repayment of the
18 loan has been accelerated in accordance with the terms of the
19 loan documents (1) as a result of the consumer's default, (2)
20 pursuant to a due-on-sale provision, or (3) due to fraud or
21 material misrepresentation by a consumer in connection with the
22 loan or the value of the security for the loan.

23 (j) A person who originates a covered loan shall not refinance
24 or arrange for the refinancing of a consumer loan such that the
25 new loan is a covered loan that is made for the purpose of
26 refinancing, debt consolidation or cash out, that does not result in
27 an identifiable benefit to the consumer, considering the
28 consumer's stated purpose for seeking the loan, fees, interest
29 rates, finance charges, and points.

30 (k) (1) A covered loan shall not be made unless the following
31 disclosure, written in 12-point font or larger, has been provided
32 to the consumer no later than three business days prior to signing
33 of the loan documents of the transaction:

34
35 CONSUMER CAUTION AND HOME OWNERSHIP
36 COUNSELING NOTICE
37

38 If you obtain this loan, the lender will have a mortgage on your
39 home. You could lose your home, and any money you have put
40 into it, if you do not meet your obligations under the loan.

1 Mortgage loan rates and closing costs and fees vary based on
2 many other factors, including your particular credit and financial
3 circumstances, your earnings history, the loan-to-value requested,
4 and the type of property that will secure your loan. Higher rates
5 and fees may be justified depending on the individual
6 circumstances of a particular consumer's application. You should
7 shop around and compare loan rates and fees.

8 This particular loan may have a higher rate and total points and
9 fees than other mortgage loans and is, or may be, subject to the
10 additional disclosure and substantive protections under Division
11 1.6 (commencing with Section 4970 of the Financial Code. You
12 ~~should consider consulting~~ *are encouraged to consult* a qualified
13 independent credit counselor or other experienced financial
14 adviser regarding the rate, fees, and provisions of this mortgage
15 loan before you proceed. *Your lender must offer you this*
16 *consultation free of charge and must obtain a signed certification*
17 *from you that you have either received counseling or have*
18 *waived your right to counseling. You may, but are not required*
19 *to, use the counselor recommended by your lender. For*
20 *information on contacting a qualified credit counselor, ask your*
21 *lender or call the United States Department of Housing and*
22 *Urban Development's counseling hotline at 1-888-466-3487 or*
23 *go to www.hud.gov/fha/sfh/hcc for a list of counselors.*

24 You are not required to complete any loan agreement merely
25 because you have received these disclosures or have signed a
26 loan application.

27 If you proceed with this mortgage loan, you should also
28 remember that you may face serious financial risks if you use this
29 loan to pay off credit card debts and other debts in connection
30 with this transaction and then subsequently incur significant new
31 credit card charges or other debts. If you continue to accumulate
32 debt after this loan is closed and then experience financial
33 difficulties, you could lose your home and any equity you have in
34 it if you do not meet your mortgage loan obligations.

35 Property taxes and homeowner's insurance are your
36 responsibility. Not all lenders provide escrow services for these
37 payments. You should ask your lender about these services.

38 Your payments on existing debts contribute to your credit
39 ratings. You should not accept any advice to ignore your regular
40 payments to your existing creditors.

(2) It shall be a rebuttable presumption that a licensed person has met its obligation to provide this disclosure if the consumer provides the licensed person with a signed acknowledgment of receipt of a copy of the notice set forth in paragraph (1).

(l) ~~(1)~~ A covered loan shall not be made unless both of the following requirements have been satisfied:

(1) The borrower has been offered loan counseling from an independent housing or credit counselor approved by the United States Department of Housing and Urban Development or the State of California.

(2) The borrower has signed a certification that he or she has received counseling on the advisability of the loan transaction and the appropriateness of the loan for him or her, or has waived the counseling option. The lender must keep a copy of any certification on file for at least three years following the certification.

(m) (1) A person who originates a covered loan shall not steer, counsel, or direct any prospective consumer to accept a loan product with a risk grade less favorable than the risk grade that the consumer would qualify for based on that person's then current underwriting guidelines, prudently applied, considering the information available to that person, including the information provided by the consumer.

A person shall not be deemed to have violated this section if the risk grade determination applied to a consumer is reasonably based on the person's underwriting guidelines if it is an appropriate risk grade category for which the consumer qualifies with the person.

(2) If a broker originates a covered loan, the broker shall not steer, counsel, or direct any prospective consumer to accept a loan product at a higher cost than that for which the consumer could qualify based on the loan products offered by the persons with whom the broker regularly does business.

~~(m)~~

(n) A person who originates a covered loan shall not avoid, or attempt to avoid, the application of this division by doing the following:

(1) Structuring a loan transaction as an open-end credit plan for the purpose of evading the provisions of this division when

1 the loan would have been a covered loan if the loan had been
2 structured as a closed end loan.

3 (2) Dividing any loan transaction into separate parts for the
4 purpose of evading the provisions of this division.

5 ~~(n)~~

6 (o) A person who originates a covered loan shall not act in any
7 manner, whether specifically prohibited by this section or of a
8 different character, that constitutes fraud.

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